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# **Policy Forum: Higher Education Funding**



**MELBOURNE INSTITUTE**  
of Applied Economic and Social Research

## ***Policy Forum: Higher Education Funding***

### **The Funding of Higher Education in Australia: Overview and Alternatives**

Stephen P. King  
Department of Economics  
The University of Melbourne

#### **1. Introduction**

Higher education funding is a perennial political football in Australia. The universities, that are predominantly government-owned institutions and rely on government funding for most of their income, argue that reduced funding is leading to a crisis in higher education. At the same time, governments of all political persuasions appear to place little importance on university funding. While the Coalition Government recently announced an increase in university research funding, the value of this package was small compared to recent reductions in the real level of funding for the university sector.

There is no doubt that the level of real funding, on a per student basis, has fallen for Australian universities over the past 20 years (see Marginson 2001). At the same time, the number of students enrolled in higher education has risen rapidly. Not surprisingly, the number of students per staff member has risen, funding for libraries has failed to match the rising costs of research publications, and Australian academic salaries have fallen well behind both Australian public and private sector salaries and equivalent academic salaries in the United States.

In this Policy Forum, three leading researchers in education consider the state of higher education funding in Australia and the potential alternatives that face both government and the universities. Overall, the Policy Forum shows that there are no simple solutions to the problems of university funding.

#### **2. Background**

There are 36 public universities in Australia. Together with two relatively small private universities, Bond and Notre Dame, these institutions provide undergraduate and postgraduate training in a wide range of disciplines. Thirty-five of the universities are established or recognised under State or Territory legislation. The exception—the Australian National University—is constituted under an Act of the federal parliament (Australian Vice-Chancellors' Committee 2000a). These institutions all rely on the federal government for most of their funding.

In 1999 there were 686267 students enrolled in higher education courses throughout Australia. Eighty-two per cent of these students were undergraduates (Australian Vice-Chancellors' Committee 2000a). These students are unevenly spread over institutions. The largest universities, such as Monash University and RMIT University, have more than 40000 students each. Smaller universities have approximately 10000 students. While most students learn 'on campus', there has been rapid growth in distance education. At one extreme, the University of Southern Queensland has approximately 20000 students, two-thirds of whom receive their education through distance learning.

Most undergraduate students pay for part of the cost of their degrees through an income-contingent loan scheme operated by the Federal Government. The Federal Government recently announced this Higher Education

Contribution Scheme (HECS) would be extended to postgraduate courses. HECS fees depend on the course undertaken by the student. For example, in 1999, the HECS charges for a full-time year of study were \$3409, \$4855 and \$5682 with courses such as law and medicine incurring the highest charge. Total HECS receipts in 2001 are estimated to be around \$1100 million (Australian Vice-Chancellors' Committee 2000b).

Public universities can offer full-fee places to overseas students and each university has discretion over the fees that it can set for overseas students. These fees are often significantly greater than the marginal cost of an extra student. For example, current overseas student fees at the University of Melbourne range from a minimum of \$13500 per year for a Bachelor of Arts degree, to \$16200 per year for a Bachelor of Commerce degree, rising to \$19700 for a Bachelor of Engineering or a Bachelor of Computer Science degree. Fees in Medicine and Veterinary Science range from more than \$20000 per year to over \$30000 per year. In recent years, overseas student numbers have risen rapidly in many courses and in 1998 overseas student fees accounted for approximately 8 per cent of university funding (Marginson 2001).

Since 1998, public universities have been able to charge up-front tuition fees for Australian students, but only for undergraduates admitted in addition to those in government-funded places. Up-front-fee places are capped at 25 per cent of the total intake of a course and, so far, only a small number of up-front-fee places have been offered (Australian Vice-Chancellors' Committee 2000a).

Total spending on higher education and government funding has been falling in real terms for much of the last two decades. On a per student basis, real funding to tertiary institutions is lower today than in 1973.<sup>1</sup> Over this time, HECS has been introduced. If these fees paid by students are excluded then real government funding per student has declined by almost 30 per cent (Australian Vice-Chancellors' Committee 2000b). Higher education spending is only 2.5 per cent of total federal government expenses, compared to approximately 7 per cent for defence and 16 per cent for health. Pro-

fessor Ian Chubb, the head of the Australian Vice-Chancellors' Committee noted in a speech in February 2000, 'that total education outlays, as a proportion of GDP, have declined from 4.9% to 4.4% over the five years to 1998' (Chubb 2000, emphasis in original).

### 3. Alternatives for Funding

At the most basic level there are two alternative sources in Australia for higher education funding—the federal government and the students.<sup>2</sup> Much of the debate over higher education funding revolves around the balance between these alternative sources, the way in which these alternative sources will provide funds, and the rules and regulations that will govern a university's access to funds.

It is unlikely that the federal government will significantly increase its funding of tertiary education on the basis of simple per student payments. Norton (2001) notes that there are strong political pressures that act against such simple funding. Higher education funding is not a priority for much of the electorate, and any political party that argues for a significant increase in payments to universities from general revenue will need to show the source of that revenue. Cutting alternative programs in health or social welfare to raise funding for universities is unlikely to be politically popular. Raising taxes to increase higher education funding is also unlikely to bring success at the ballot box.

Any significant increase in federal government funding will be tied to an explicit method for raising the funds, such as HECS. Chapman (2001) argues that an income-contingent loan scheme operated by the government has many benefits over alternative funding arrangements. He also argues that universities should have more autonomy to set the course fees under HECS. Norton argues that universities should be allowed to charge top-up fees to students, organised through an income-contingent loan scheme.

Marginson (2001) notes the potential danger of increased HECS funding for the course mix offered by universities. Increased HECS funding will lead to increased demand for business, engineering and other 'marketable' degrees.

These studies provide a direct return to students through high paying employment after graduation. Marketable degrees, however, are unlikely to provide significant public benefits that are not captured by the student. The economic case for public funding of higher education rests, at least in part, on the ability for university studies to create social benefits that are not captured by the student through higher wages. Increased HECS funding will not increase the provision of socially beneficial but privately unprofitable courses.

Chapman argues strongly against either direct student fees or the use of private sector loan schemes. While there are many problems with such systems, it seems undesirable to dismiss these schemes out of hand. For example, if we follow Marginson, and consider some degrees as more marketable than others, then it seems unreasonable that the government should provide the same form of funding to all undergraduates. For example, should a degree that might involve significant benefits to society, such as studies in Australian history or agricultural science, involve the same form of funding as a highly marketable accounting degree? It seems sensible that if the government is to continue to be the major source of funds to universities then it should also more tightly target those funds. If the government believes that some degrees are more worthy of public support than other degrees, then it should allocate HECS places to those worthy areas of study. In contrast, for studies that are aimed at achieving a marketable professional qualification, particularly where studies are strongly guided by professional associations, there seems little argument for public funding.

In a limited way, the government already discriminates in fee payments between different areas of study through the three tiers of HECS. Marketable degrees in Law and Medicine face the highest HECS charges while studies that receive less market reward such as nursing and humanities pay lower fees. It could be argued that this discrimination should be broadened. Students studying in areas providing significant external public benefits might have access to an interest-free income-contingent loan and direct government funding

for part of the cost of their studies. Students studying in highly marketable areas might have no access to HECS, or if HECS were available it would involve a market-based interest rate. HECS repayments might also begin at a lower income level for such marketable degrees.

A scheme of targeted funding could involve significant deregulation of the fees charged by universities. For marketable degrees, demand and supply could largely determine the fee. Universities with high quality teaching and smaller classes would be able to charge higher fees than universities with poor teaching and large classes. As Chapman notes, some care would be needed to make sure that fair competition existed between public universities. For example, those universities located on prime CBD real estate would face a significant advantage over their suburban and country equivalents. Such bias might be addressed by requiring universities to pay a market-based rent on their campuses to the government.

For subsidised areas of study, the government might still need to set the basic fee to avoid opportunistic behaviour by universities. Funding on a per student basis would have to at least cover the true costs of the students, otherwise universities would cut back these socially desirable areas.

A differentiated system of funding and fees would require the government to decide which areas of study provide the greatest social spill-overs. Such a decision would be difficult and controversial. Every area would claim its importance. Business faculties would proclaim their benefits to Australia's international competitiveness. Science faculties would cite the links between research and development and economic growth. Engineering would mutter darkly about lives lost when a bridge or building collapses. While deciding appropriate levels of support for different areas of study will be difficult, this is not a reason to avoid the task and simply treat all areas of study as essentially identical.

Many of the current funding concerns that face universities reflect their changing place in Australian society. As Chapman notes, in the early 1970s few young Australians studied at university. The number of young Australians

studying at university rose rapidly during the 1990s. University education is no longer a luxury enjoyed by an intellectual elite but a necessary precursor to the job market for many young people. This changing role is reflected in the size and number of universities. It is also reflected in the growth of marketable undergraduate courses. The changing role of universities has affected their ability to provide basic research. Teaching and research can conflict. While teaching and student numbers provide the funds for a department, research is often the key criterion for promotion.

Australian universities are now trying to provide a number of important, distinct social services but are locked into uniform institutional and funding structures. Universities provide both professional qualifications and generalist studies. Staff range from exceptional teachers with little or no interest in basic research, to world-class researchers. Some students view their degree simply as a meal ticket or an entrée into a high paying professional career. Other students simply wish to expand their knowledge and to improve their own and society's understanding of the world. The structure of Australian universities and their funding need to reflect and accommodate these different roles.

A differentiated system of fees and funding for degrees would create flexibility for the universities as well as more tightly focusing government expenditure. Over time, the universities might respond by dividing into two separate groups. One group would provide market-oriented degrees, potentially on a full-fee-paying basis. The other group would concentrate on socially desirable studies, possibly through a less structured generalist degree of the type taught at the elite US schools such as Harvard and Princeton universities. Alternatively, universities might alter their internal structures to reflect the incentives created by differentiated funding.

Reducing or eliminating government subsidies for market-oriented degrees that provide few social spillovers would free up significant funds that could be used for basic research. These funds could be allocated through a competitive process, such as the current Australian

Research Council grants. They could also be allocated as both start-up grants to new researchers and as ongoing research grants to successful researchers. For example, research funds could be allocated at least in part on the basis of successful publication in high quality international research journals. Academics providing important research in any area would be able to apply for funding.

#### 4. Conclusion

The role of Australian universities has changed beyond recognition in the past 30 years. As a result, universities are now attempting to fill a variety of important but distinct social roles. They provide professional qualifications as well as generalist studies; basic research together with fee-for-service consulting; and teaching ranges from undergraduate humanities and science to in-house corporate training. These disparate and sometimes conflicting roles have made the traditional government funding arrangements obsolete.

This Policy Forum brings together a group of articles that present alternative options for university funding. While some authors see the solution as lying in increased direct government funding, others look to student fees, possibly through a government-operated income-contingent loan scheme, to provide long-term financial security to universities. In my opinion, both of these alternatives are relevant and important. However, the problems with university funding reflect deeper internal conflicts within universities that have been created by the changing role of these institutions.

The funding problems for universities are unlikely to be overcome unless the distinct and different roles now played by universities are recognised. For undergraduate teaching, it must be recognised that universities no longer teach a small elite group of young Australians. They provide a wide range of teaching services, including professional qualifications and marketable degrees as well as studies in areas that provide spillovers to broader Australian society. Government funding and student fees need to recognise the range of different undergraduate areas of studies. Funding needs to be

focused on areas providing social benefits rather than simply marketable qualifications. A necessary consequence is that government funding and student fees must differ significantly between areas of study.

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### Endnotes

1. This is reported in terms of 'planned effective full-time student units'. See Australian Vice-Chancellors' Committee (2000b).

2. Corporate sponsorship is a growing source of funds, but it is unlikely to provide more than a very small fraction of university funding in the near future.

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***Policy Forum: Higher Education Funding*****Australian Higher Education Financing: Issues for Reform**

Bruce Chapman\*

Centre for Economic Policy Research  
The Australian National University**1. A Recent History of Australian Higher Education Financing**

The financing of Australian higher education has undergone radical change since the early 1970s. At that time the Federal Government provided practically all funding, and until the late 1980s there was little political support for change. However, over the last decade there has been a very significant move towards greater private contributions, particularly student tuition charges.

Further, since the change in Federal Government in 1996 the levels of student charges and the nature of their payment have changed. There have also been policy moves over the last few years promoting greater institutional autonomy and flexibility with respect to charging. The current arrangements are almost unrecognisable compared to those in place under the Whitlam Government.

**1.1 Fee Abolition in 1973**

In the early 1970s up-front fees were paid by some students. These were abolished by the newly elected Federal Labor Government, in 1973. This policy change had two key motives.

First, fees were believed to erect barriers to participation in higher education by the poor. Thus their abolition was seen to be important in

improving the access of the disadvantaged to better lifetime opportunities. Second, fee abolition was symbolically important as a reflection of the Labor Government's social democratic credentials.

The abolition of university fees at this time had no discernible effects on the socioeconomic composition of higher education students,<sup>1</sup> for two reasons. First, only a small proportion of students (20–25 per cent) paid fees, since the great majority had either Teacher's College or Commonwealth Scholarships. Second, because secondary schooling retention rates to the equivalent of Year 12 were very low at the time (less than 30 per cent), most prospective students from poor families had left the education system well before university.

**1.2 The Higher Education Administration Charge**

The Coalition Government of 1975–83 made no significant changes to university financing. However, the Labor Government introduced the so-called Higher Education Administration Charge (HEAC) in 1986.

HEAC was an up-front fee and its introduction is a watershed: it introduced user-pays. The charge was small—\$250 (in 1986 terms)—and did not vary with respect to course load. There is some evidence that it had a small negative effect on mature-aged part-time enrolments.<sup>2</sup>

HEAC was symbolically important as a user-pays perspective had been rejected by

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Australian governments of different persuasions for over a decade. As well, HEAC showed the intention of several Cabinet Ministers (notably Peter Walsh and John Dawkins) to address what they thought was a critical equity issue: not charging for higher education is regressive because the subsidy from all taxpayers—including the poor—goes mainly to those from advantaged families. The pejorative labelling of 'free education' as 'middle class welfare' was a major theme at the time.

### 1.3 Higher Education Contribution Scheme

The Higher Education Contribution Scheme (HECS), recommended by the Wran Committee set up by John Dawkins in 1988,<sup>3</sup> was adopted in 1989. This was a universal charge to undergraduate students of \$1800 (in 1989 terms), with a unique feature: students could defer payment until their future incomes reached a particular threshold, with no real rate of interest being charged on the debt. This was the world's first income-contingent charge for higher education,<sup>4</sup> a policy arrangement that has since been adopted or recommended in many other countries.<sup>5</sup>

HECS came about because the government wanted to increase higher education enrolments but was not prepared to pay for the increased expenditure through taxation. Most importantly, 'free education' was seen to be regressive and unfair.<sup>6</sup>

While many critics of HECS alleged at the time that the new system would have major adverse consequences for the access of the disadvantaged, this has not turned out to be the case. Some part of HECS' success on this level relates to the significant advantages of the nature of repayment, an issue analysed below.

### 1.4 1996–97 Budget Changes

In its first Budget the Coalition Government announced four significant financing modifications:<sup>7</sup>

- all charges were increased, by around 40 per cent on average.

- the income thresholds for repayment of the debt were reduced considerably—for example, the annual income initiating the first repayment fell from about \$30 000 to about \$21 000 (in 1996 terms).
- the uniform charge was replaced with three levels.
- universities were allowed to set whatever level of fee they wanted for undergraduates not accepted under existing HECS quotas.

The most significant change to HECS relates to the repayment thresholds. Because the whole structure was moved down, all people repaying HECS—most of whom have graduated—now pay more in net present value terms, because they would have less of the subsidy implicit in an interest-free loan. Chapman and Salvage (1998) estimate that this meant an average increase in effective repayment obligations of about 10 per cent.

The new three-tier charge structure was set with reference to a combination of course costs and what seems to be a presumption of the income advantages of different degrees. For example, one of the lowest cost courses (Law) was accorded the highest charge, and one of the high cost courses (Nursing) was accorded the lowest charge. Interestingly the Wran Report also suggested a three-tier charge structure, but with the charges reflecting course costs only.<sup>8</sup>

Allowing universities price discretion for additional students was a radical departure from centralised fee control. While so far there has been little take-up of this option, it represents the most significant movement towards institutional pricing autonomy in the history of Australian higher education (Chapman 1997).

## 2. Options for Higher Education Financing

Several different policy approaches, currently in operation internationally, are now analysed with respect to their social and economic implications.



### 2.1 A No Charge System

Many, although increasingly fewer, countries do not charge for higher education. What this means can be understood through reference to standard principles, now explained briefly.

A role for government is to help ensure the production of optimal quantities of goods and services. In some circumstances this requires public subsidies equal to the marginal value of the externality associated with an activity.<sup>9</sup>

All charging systems implicitly place a value on externalities. For example, having no charge suggests that societal benefits at least equal the size of the subsidy, and, implicitly, that graduates receive no direct benefits. While there is little agreement on the size of externalities, it is certainly clear that the process delivers important private benefits to graduates.<sup>10</sup>

The other issue related to not charging for higher education is that of equity. There is no doubt that university students are more likely to come from privileged backgrounds, and it is also true that graduates do well in the labour market. Thus a no charge system is unquestionably regressive.

### 2.2 Up-Front Fees with No Financial Assistance

If there should be a charge, how should it be paid? In this context the critical issue relates to a major borrowing problem, often referred to as 'capital market failure'.

The important point is that banks are reluctant to loan to students because of problems associated with default. An education loan is risky for a bank because, in the event of default—and unlike with respect to a housing loan—the bank has no collateral to sell. This implies that, without assistance, banks will not be interested in the underwriting of human capital investments.

There will be three important effects: a loss of talent, and thus a cost to the whole society; a loss of opportunity to individuals; and a cementing of the nexus between family background and a person's lifetime income, meaning that such a system is regressive.

### 2.3 Up-Front Fees with Bank Loans

A possible solution to the capital market problem used in many countries involves government-assisted bank loans to students with low family incomes. The most important form of public sector support is the guarantee of repayment of the debt to the bank in the event of default. There are several problems here.

The first is that access to loans is usually means-tested on the basis of family income. This presumes equal access of individuals to family finances. But those in charge of the distribution of household finances may not have the prospective student's view of the value of education. If so, outcomes will not be optimal.

The second problem is default. For the government this is costly since bank-financed student loans default rates are very high.<sup>11</sup> And if there is a guarantee that defaults will be paid for by the government, banks will put little effort into debt recovery.

Students also face a default issue. This is that some may be reluctant to borrow for fear of not meeting future repayment obligations, with concomitant damage to a person's credit reputation (and thus access to future borrowing, for example, for a house). A consequence is that some eligible prospective students will not be prepared to take bank loans.<sup>12</sup> This problem can be traced to the fact that bank loan repayments are insensitive to the borrower's financial circumstances.

### 2.4 Income-Contingent Charging Mechanisms

A final approach to student financing involves income-contingent charges, such as HECS. The attraction of income-contingent schemes is that they can be designed to avoid all the problems associated with alternative financing policies outlined above.<sup>13</sup>

First, there is no concern with intra-family sharing so long as the scheme is universal. Second, given an efficient collection mechanism, there is no default issue for the government.<sup>14</sup> Third, because repayments depend on incomes, there should be no student default concerns.

HECS has been in operation since 1989, and there is now considerable evidence concerning its consequences<sup>15</sup> for both demand for higher education and the access of the poor: the bottom line is that there have been negligible effects in both areas.<sup>16</sup>

### 3. Current Issues in Australian Higher Education Financing: Towards a Solution

What now follows explores a subset of the many contemporary challenges for university funding: should universities have discretion to set charges for students? should the government limit the extent of university price autonomy? and what are the right reform directions?

#### 3.1 *The Background to a Case for Institutional Price Flexibility*

It is unlikely that future governments will markedly increase subsidies for higher education. And given that there are currently strong financial pressures on universities, there is a case for increased institutional price flexibility. Two factors leading to this situation are now explained.

- Fiscal parsimony

Over the last two decades most Australian and OECD governments have endorsed low-tax fiscal positions. There is no reason to believe that this will soon change.

An indirect implication for Australian public sector universities is that academic real wages have fallen significantly.<sup>17</sup> This means decreases over time in the relative attractiveness of academic employment and thus a diminution in the quality of applicants and resignations of some of the best staff. Concomitantly the average quality of academic staff has been falling.

- Enterprise-based bargaining

There has been a government-initiated movement over the last ten years or so towards enterprise bargaining in universities. However,

unlike what this means for the private sector, there are no instruments to make the arrangement operational; unlike private firms universities cannot vary prices or institute profit-sharing relationships.

That is, Australian universities face a fairly fixed pie. A pay increase for all staff, for example, is likely to mean job losses. In the context of governments not being willing to maintain real levels of higher education expenditure, an enterprise bargaining system inevitably exerts significant pressure for independent funding sources.

The above factors mean that something has to give, and one candidate is the introduction of some institutional revenue autonomy, with the additional resources being delivered directly to the institutions. This would promote competition, which has several potential benefits, now explained.

Australia is now in a situation whereby universities supply services for a large and diversified market. Higher education is no longer elite and small, and there will increasingly be opportunities for specialisation in terms of both subject matter and the targeting of particular consumers.

In this context quality and price differentiation promote the case for allowing universities to offer services and prices reflecting their circumstances and goals. This would allow more choice for both providers and students, and has the potential to improve service delivery.

But if universities are to have some discretion over prices, two questions arise: should there be price regulation? and, how can the movement to greater institutional pricing autonomy be achieved without compromising students' access?

#### 3.2 *Towards Reform: Price Regulation and the Payment Mechanism*

There is perhaps now a case for greater institutional autonomy with respect to pricing. Universities could offer different charges to encourage competition and improved resource allocation.

This raises two critical issues: the extent to which universities should be free to set prices;

and what payment mechanisms should be available.

### 3.2.1 Problems with Unfettered Price Setting

There are two important reasons to be concerned about unfettered price competition between Australian universities. The first is that the extent to which institutions will be able to benefit from price discretion will be a result of their location and history. For example, the Universities of Sydney, Western Australia, Adelaide and Melbourne are located in prime areas of their respective cities, and this gives them a significant commercial advantage. The fact that universities do not pay rent means that the playing field is not level.

Further, an important part of universities' relative standing is the result of many years of public subsidy. Reputations have been built up from these subsidies, implying that there might be important rents accruing to some universities from unfettered price competition.

The bottom line is that allowing free market principles in the pricing of higher education services in Australia is premature until convincing analysis of the likely consequences is available. This means that, at least in the short term, the government will need to set boundaries on the level of price changes.

### 3.2.2 Payment of Charges

For reasons documented in Section 2 it is critical that any moves towards greater institutional price flexibility have to be accompanied by student access to a HECS-type financing scheme. Indeed, if this does not happen, and universities are simply allowed to set prices to improve competition, the net effects will unambiguously be negative.

It is not difficult to devise a scheme characterised by increased competition that also has an income-contingent repayment basis. For example, the government could specify broad bands of charges by discipline and allow universities to set prices up to 25 per cent above<sup>18</sup> specified levels. At enrolment students would

commit to repaying the debt through HECS, or pay the charge directly to the university with the current 25 per cent discount.<sup>19</sup>

In the circumstance of a student choosing the pay-later option, the government would pay the university the additional charge amount (discounted by 25 per cent). In the future, on average, the government will receive charge revenues from pay-later students which will be close to the net present value of the discounted charge. Many variations of this approach are possible, and the scheme could take the forms described in Karmel (2000) or Miller and PinCUS (1998).

### 3.3 Conclusion

There are good reasons to reform the current system. Public funding is sparse and will remain so, irrespective of which party is in government, and the current arrangements are not very sensitive to issues of allocative efficiency. This can be promoted by allowing increased institutional flexibility with respect to pricing, with the additional fee revenue being delivered directly to the institutions. Changes along these lines are likely to promote diversity and help arrest the decline in academic employment conditions.

However, there are important reasons to limit the extent to which universities are able to vary prices. Moreover, the case for the provision of income-contingent financing support for students is overwhelming. Irrespective of the nature of other financing reform, any movement towards up-front fees and away from HECS will undoubtedly result in a poorer policy prescription.

## 4. A Postscript: The Government's Plan for Postgraduate HECS Loans

In January 2001 the Government announced, as part of its Innovation Statement, that an income-contingent loan would soon be available to all fee-paying non-research postgraduate students to cover current up-front charges. In a subsequent interview<sup>20</sup> the Minister, David Kemp, offered details of the new scheme.

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#### 4.1 The Plan Explained and Motivated

The main features are that there will be no limits on the amount a student can borrow; the loan would be repaid according to the current HECS arrangements; and universities would remain free to set postgraduate charges.

As stressed above, there are very good reasons for an income-contingent charge mechanism for postgraduate degrees. Allowing the payment of up-front fees with the use of HECS-style loans will increase the access of the relatively disadvantaged to postgraduate studies. This will have the two important effects of increasing the pool of talent available for postgraduate studies and expanding the access of the system to the less privileged.

In principle, this policy change should be applauded. Moves away from up-front fees and towards income-contingent repayment reflect correct principles of reform for the Australian higher education system. There are some interesting issues with respect to the form of this particular proposal, however.

#### 4.2 Some Implications of the Plan for Postgraduate Charge Levels

The Minister has argued that competition would restrict the extent to which universities would commensurately increase postgraduate fees, saying: 'We're not expecting that there will be any significant change in fees as a result ...'.<sup>21</sup> However, this is more complicated than is apparent.

In analysing the implications of this policy change it is critical to recognise that the postgraduate charge facing a student who can pay with an interest-free loan is necessarily different to the fee received by the university. This is because the university receives the money at the time of enrolment, but the student repays the debt later. Critically, the absence of a real rate of interest on the debt means that in financial terms the student will necessarily be facing a lower impost than the actual charge. In other words, there will be a government-financed subsidy.

The extent of the subsidy depends on how long before the student begins to repay the

postgraduate loan, and the length of time taken to repay it once repayments begin. That is, among other things, the subsidy depends on students' expected future incomes and the level of outstanding HECS undergraduate debt at the time the postgraduate loan is taken. The latter is critical because the postgraduate obligation will only start to be repaid once other HECS obligations have been met.

For example, students starting a postgraduate qualification when they have a large undergraduate HECS debt will have a long period of subsidised benefit, and thus will implicitly face a relatively small charge in true financial terms. On the other hand, postgraduate students with no HECS debts, and already earning, will receive relatively small subsidies.

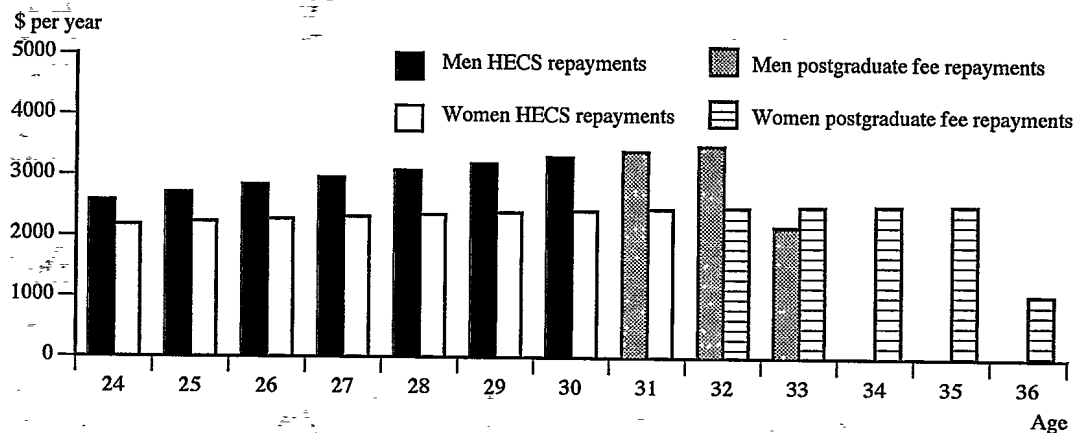
Unambiguously, however, if the nominal size of the charge remains unchanged, the new scheme financially benefits all students taking the loan. This has a very important implication for a university's postgraduate pricing policy in the context of the government allowing complete postgraduate fee flexibility. What then is likely to happen?

The answer is that because these new arrangements mean that the effective charges faced by most students are now lower than before, universities will be able to increase the fee charged. Importantly, these fee increases, while real for the university, are not necessarily true increases for students who can defer payment since they have access to the (real) interest-free loan.

The existence of competition between the universities will have limited impact on the above. After all, all universities will have the benefit of students now facing lower true charges, and the system will deliver new nominal charges reflecting this fact.

With the presumed higher charges the universities will be unambiguously better off, since they will be receiving the additional revenue at the time of student enrolment. Prospective postgraduate students are also likely to be advantaged, but the extent of their benefit will be determined by how large the presumed nominal fee increases turn out to be. The costs of the subsidy will be financed by the public sector.

Figure 1 Repayments of HECS Undergraduate and Postgraduate Debt



#### 4.3 Estimates of the Subsidy

An obvious way to work out the size of the subsidies implicit in the new postgraduate policy approach is through the application of human capital techniques with respect to the net present value of charges under the planned arrangements. This is now reported from the use of cross-sectional data with information on individuals' age, earnings, education and sex.

The 1994-95 Australian Bureau of Statistics' Income Distribution Survey is an apposite data set available to address the issue. For this exercise some simple counterfactuals have to be defined. The first is as follows.

Imagine that a person has completed a four-year undergraduate degree begun at age 18 and completed at age 22. A middle-range HECS debt would be \$19720. Further, it is assumed that the student chooses to undertake two extra years of postgraduate study for which there is a charge of \$5000 per year.

Our hypothetical students will have the benefit of not paying any real interest on the additional debt until their existing HECS debt is repaid. Assuming that they earn the average incomes of men and women with a higher degree (the earnings profiles being shown in Appendix 1) it is possible to illustrate when the repayments occur, and these are shown in Figure 1.

The data show that for the examples chosen, men and women will start to repay the postgraduate loan at ages 31 and 32, and will finish the repayments at ages 33 and 36 respectively.

These data can be converted into calculations of the net present value of the charges, calculated at age 22. The results can be compared to the net present value of the charges paid upfront to calculate the implicit subsidy, now shown in Table 1.

The data from Table 1 show that for some students there is a very large subsidy implicit in the Government's plan: in the order of 41-47 per cent.

Two other examples are now presented. They are for postgraduate students with no HECS debts beginning their courses at age 22 and age 32 respectively. The results are shown in Table 2.

Table 1 Net Present Value of a \$10000 Postgraduate Debt, HECS Unpaid

|                               | Men    | Women  |
|-------------------------------|--------|--------|
| Net present value of the debt | \$5942 | \$5329 |
| Implicit subsidy (per cent)   | 40.6   | 46.7   |

Table 2 Net Present Value of a \$10000 Postgraduate Debt, HECS Paid

|  | Men    | Women  |
|--|--------|--------|
| Scenario 1: Paid off HECS debt before postgraduate studies beginning at age 22 |        |        |
|  | \$8137 | \$7971 |
| Subsidy (per cent)   | 18.6   | 20.3   |
| Scenario 2: Paid off HECS debt before postgraduate studies beginning at age 32 |        |        |
|  | \$8266 | \$8052 |
| Subsidy (per cent)   | 17.3   | 19.5   |

The subsidies of around 17–20 per cent are much lower than would be the case for students with high outstanding undergraduate HECS debts. It is also critical to note that a very large number of current postgraduate students are both part-time and aged over 30, implying strongly that they are full-time workers already earning over the HECS repayment threshold. For these students the subsidies will be somewhat lower than for Scenario 2,<sup>22</sup> and for other prospective students there will be no subsidy at all.<sup>23</sup>

Even given that there is a large range of subsidies, and accepting that for many students already earning high incomes these subsidies will be low, it is still the case that on average under the new system the effective charges will be lower than before. Thus the tendency will be to increase the pressure for universities to increase (nominal) postgraduate charges. Since all universities will face similar increases in the effective demand for their services from the new arrangements, the role of competitive forces is unlikely to stop this happening. While this is not obviously a bad or a good thing, the critical issue is what then happens.

able to assist postgraduates to pay fees is an excellent development in Australian higher education financing policy. It will improve access for prospective postgraduate students, and will as a result mean that there will be less wasted educational talent and a better workforce. It will also improve significantly the opportunities for poorer prospective students.

However, the new scheme implies that a sizeable proportion of students will receive a government subsidy which will increase effective demand for the service. This is likely to facilitate nominal charge increases, meaning that universities will receive higher charge revenues. The government will thus be subsidising both students and universities more than currently. It is of interest that a reasonable response to this issue would be the offering of a 25 per cent discount for those paying up-front, which is the way undergraduate HECS works. In practice this would be straightforward: the government would pay the fee to the university for the student and the student would agree to repay through the tax system a nominal sum which is 25 per cent higher.

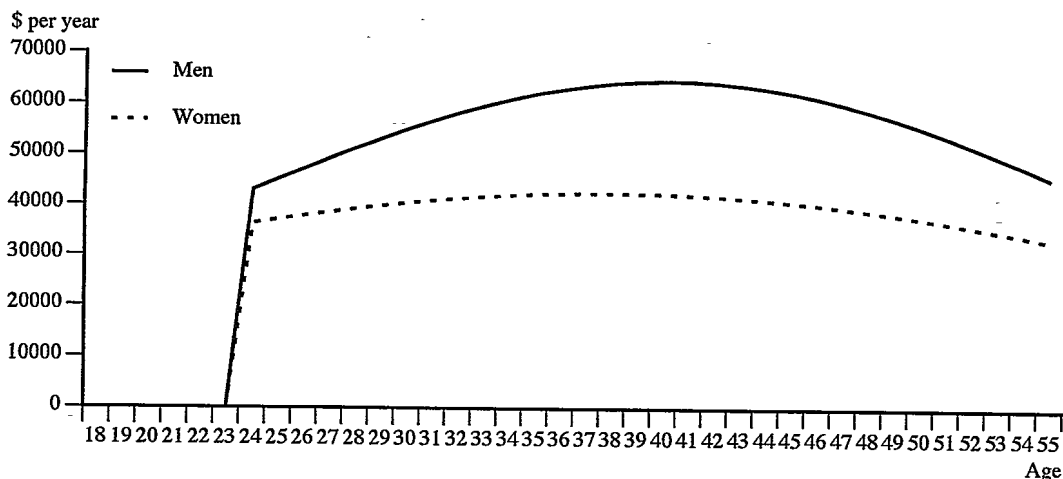
April 2001

#### 4.4 Conclusion

The Government's recent announcement that income-contingent loans will be made avail-

#### Appendix 1: Age Earnings Profiles for Postgraduates

Figure A1 Age Earnings Profiles: Postgraduates



Source: Derived from Australian Bureau of Statistics, 1994–95 Income Distribution Survey, Cat. no. 6523.0.

### Endnotes

1. See Committee on Higher Education Funding (Wran Report) (1988).
2. See Robertson, Sloan and Bardsley (1989).
3. See the Wran Report (1988).
4. For an analysis of the background to HECS, see Edwards, Howard and Miller (2001).
5. Income-contingent loan schemes for higher education are now in place in New Zealand, the United Kingdom, Ghana, and Namibia, and have been recommended by the World Bank, or are currently being implemented in Ethiopia, Rwanda, Hungary and Malaysia.
6. For further analysis of the background to the policy, see Chapman (1997).
7. For an analysis of the effects of these changes, see Chapman and Salvage (1998).
8. For a critical commentary on these changes, see Chapman (1997).
9. The nature and importance of higher education externalities are documented in Chapman and Withers (forthcoming).
10. See the Wran Report (1988).
11. Harrison (1996) notes that in US Propriety Colleges the default rate is as high as 50 per cent. The average default rate for student loans is around 15–30 per cent (Wran Report 1988).
12. For an analysis of this issue, see Chapman (1997).
13. For a theoretical analysis, see Chapman (1997).
14. Harding (1995) calculates that the total repayments remaining uncollected because of the nature of HECS would be of the order of 15–25 per cent for the original scheme (when the repayment conditions were much more

generous for the student (before the 1996–97 changes)).

15. See the annual reports from the Higher Education Council (1990–2000), Chapman and Smith (1985), Chapman (1997), and Andrews (1999).

16. For a summary, see Chapman (1997).

17. For example, the salary of a Level E Professor has decreased by around 25 per cent in real terms over the last 20 years.

18. It is of interest to note that some institutions might be encouraged to charge low prices to encourage the establishment of a market niche.

19. For details of how this might work, see Chapman (2001).

20. See Illing (2001).

21. See Illing (2001, p. 35).

22. The subsidies will be of the order of 10–15 per cent. See Chapman (2001).

23. For those students who currently pay the up-front fee to qualify for a self-education tax deduction there will be no subsidy.

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**Policy Forum: Higher Education Funding****Trends in the Funding of Australian Higher Education**

Simon Marginson\*

Monash Centre for Research in International Education

Monash University

**1. Introduction**

This article situates the funding of Australian higher education in historical perspective. Three time frames are used: the building of a publicly financed national system of higher education from 1961 to 1988; the creation of a mixed (public and private) funded national system from 1989 to 1995; and the current policy framework after 1995. The article uses Australian Bureau of Statistics (ABS) and Commonwealth data to map trends in funding levels and funding sources. Then it reflects on trends in the resource conditions underlying the quality of teaching and research, shaped by successive changes in funding levels and in financial incentives. Finally, the article looks briefly at investment in Australian higher education in comparison with other OECD countries.

These trend data are not designed to generate predictions. The future of higher education funding is not necessarily the same as the past (Dow and Hillard 1995). One recalls Keynes's criticism of Tinbergen's use of time series data: 'the economic environment is not homogenous over a period of time (perhaps because non-statistical factors are relevant)' (Keynes 1973, p. 308). The point is particularly relevant in sectors such as higher education, in which in-

puts are subject to arbitrary and determining 'non-statistical factors' in the form of public policies. Nevertheless, time series data facilitate policy judgement in ways other than prediction. Such data help to explain the present, displaying the consequences—intended and unintended—of accumulated past decisions by governments, institutions and individuals. In higher education the costs and benefits are often long-term in character. Australian universities may again be on the brink of a major policy shift. A renewed interest in education and science is evident (Beazley 2001; Howard 2001). If so, decisions made in the near future will shape the national capacity in education and research for decades to come.

**2. ABS Data on Public Investment in Higher Education since 1961**

The ABS provides a consolidated data series on public expenditure in education dating from 1961–62 (ABS 2000a). The modernisation of higher education and the construction of a national system derived from the Murray and Martin reports under Menzies. Between the late 1950s and the mid 1970s, ten new universities were built, enrolments grew six-fold and the Commonwealth assumed full funding responsibility, abolishing all remaining tuition fees. National investment in higher education reached a late-Keynesian high of 1.50 per cent of GDP in 1974–75 under the Whitlam Labor Government (Table 1, see also Marginson 1997a), placing Australia in the top third of OECD countries. Australian academic salaries

\* Professor Simon Marginson is the co-author with Mark Considine of *The Enterprise University: Power, Governance and Reinvention in Australia*, published by Cambridge University Press (2000).

were equivalent to US academic salaries in Purchasing Power Parity (PPP) terms, and the overall student to academic staff ratio was 11.7. The infrastructure created in the period of

system-building was sufficiently robust to sustain another 20 years of growth in student participation, amid increasing strains, despite the decline in national investment.

**Table 1 Government Outlays on Higher Education, Constant 1989-90 Prices, Australia: 1961-62 to 1997-98**

|         | Government (public) outlays on higher education:<br>(\$million 1989-90 prices) |                                 |  |       | GNP/GDP<br>(\$million<br>1989-90 prices) | Public outlays<br>as a share of<br>GNP/GDP<br>(per cent) |
|---------|--|---------------------------------|--|-------|--|--|
|         | Final<br>consumption<br>expenditure  | Fixed<br>capital<br>expenditure | Expenditure<br>on benefits to<br>individuals | Total |  |  |
| 1961-62 | 397  | 221                             | 137  | 748   | 124481                                   | 0.61   |
| 1962-63 | 402  | 205                             | 159  | 765   | 133303                                   | 0.57   |
| 1963-64 | 460  | 212                             | 168  | 854   | 142577                                   | 0.60   |
| 1964-65 | 567  | 241                             | 184  | 1000  | 151865                                   | 0.66   |
| 1965-66 | 614  | 262                             | 221  | 1097  | 155048                                   | 0.71   |
| 1966-67 | 673  | 293                             | 253  | 1227  | 166000                                   | 0.74   |
| 1967-68 | 826  | 310                             | 258  | 1407  | 172368                                   | 0.82   |
| 1968-69 | 906  | 331                             | 300  | 1550  | 188363                                   | 0.82   |
| 1969-70 | 982  | 381                             | 333  | 1702  | 199530                                   | 0.85   |
| 1970-71 | 1158   | 322                             | 390  | 1870  | 209605                                   | 0.89   |
| 1971-72 | 1265   | 397                             | 455  | 2122  | 217063                                   | 0.98   |
| 1972-73 | 1361   | 370                             | 534  | 2274  | 222832                                   | 1.02   |
| 1973-74 | 2080   | 401                             | 426  | 2916  | 235844                                   | 1.24   |
| 1974-75 | 2609   | 587                             | 367  | 3584  | 238790                                   | 1.50   |
| 1975-76 | 2675   | 440                             | 378  | 3505  | 245396                                   | 1.43   |
| 1976-77 | 3008   | 368                             | 357  | 3735  | 254095                                   | 1.47   |
| 1977-78 | 3018   | 305                             | 302  | 3631  | 256674                                   | 1.41   |
| 1978-79 | 2919   | 326                             | 257  | 3506  | 270391                                   | 1.30   |
| 1979-80 | 2847   | 276                             | 216  | 3343  | 276289                                   | 1.21   |
| 1980-81 | 2879   | 221                             | 203  | 3309  | 284273                                   | 1.16   |
| 1981-82 | 2922   | 200                             | 170  | 3296  | 294404                                   | 1.12   |
| 1982-83 | 2915   | 218                             | 162  | 3301  | 287646                                   | 1.15   |
| 1983-84 | 2921   | 231                             | 181  | 3349  | 303286                                   | 1.10   |
| 1984-85 | 2773   | 207                             | 192  | 3184  | 318955                                   | 1.00   |
| 1985-86 | 2960   | 198                             | 197  | 3352  | 328927                                   | 1.02   |
| 1986-87 | 2978   | 262                             | 238  | 3520  | 336231                                   | 1.05   |
| 1987-88 | 2887   | 325                             | 257  | 3448  | 357077                                   | 0.97   |
| 1988-89 | 2449   | 305                             | 447  | 3181  | 371564                                   | 0.86   |
| 1989-90 | 2271   | 318                             | 452  | 3048  | 383497                                   | 0.79   |
| 1990-91 | 2619   | 479                             | 557  | 3636  | 384323                                   | 0.95   |
| 1991-92 | 2830   | 471                             | 660  | 3943  | 386604                                   | 1.02   |
| 1992-93 | 2791   | 700                             | 728  | 4220  | 402816                                   | 1.05   |
| 1993-94 | 2694   | 803                             | 738  | 4248  | 417318                                   | 1.02   |
| 1994-95 | 2933   | 798                             | 778  | 4528  | 436657                                   | 1.04   |
| 1995-96 | 2718   | 799                             | 833  | 4334  | 456739                                   | 0.95   |
| 1996-97 | 2820   | 829                             | 818  | 4451  | 471394                                   | 0.94   |
| 1997-98 | 2880   | 782                             | 796  | 4420  | 494375                                   | 0.89   |

Source: Revised and unpublished data from the ABS.

Until the late 1980s the Commonwealth continued to provide 90 per cent of higher education funding, but the level of funding was frozen by the Fraser Coalition Government that followed Whitlam, and fell slightly under the Hawke Labor Government. As enrolment growth accelerated in the second half of the 1980s, driven by rising aspirations for education and by credentialism in the professions, public funding per unit of student load<sup>1</sup> declined sharply, from \$15307 in 1975–76, and \$12827 in 1983–84, to \$8324 in 1989–90 (Table 2: all price data are in constant 1989–90 dollars). By then academic salaries were at two-thirds of US salaries in PPP terms and student-staff ratios were rising. As Table 1 shows, government final consumption expenditure peaked at \$3.0 billion in 1977–78 and never reached that level again, although student load more than doubled in the next two decades.

The ABS defines government final consumption expenditure in higher education as net outlays by general government for current purposes such as salaries, intermediate services, power, library and educational materials; that is, government-source outlays which do not result in the creation of capital assets or land (ABS 2000a). Together with revenue via the Higher Education Contribution Scheme

(HECS), government final consumption expenditure is still the main source of the academic resources that underpin teaching and research. While expenditures on these academic resources are recorded as current expenditures, in one sense they are also akin to fixed capital investment, in that the benefits are partly drawn on in years subsequent to the current year. Academic resources (especially the combined knowledge-capacity of the individuals working in universities) constitute an ongoing social infrastructure which tends to accumulate—or erode—over time, depending on the degree to which that capacity is being augmented by current outlays. It is in this respect that the aggregate government expenditure on higher education, capital and current expenditures taken together, is described in broad terms as ‘public investment’ in higher education. Similarly, private expenditures on higher education in the form of tuition and other current costs are often described as private investments in future earning capacity.

Public investment as a proportion of GDP reached an historic low of 0.79 per cent in 1989–90, while the Dawkins reforms were being implemented, including further expansion on the basis of mixed (public and private) funding. The continued scarcity of public funds provided universities with a powerful incentive to work the new markets that had opened up in international and postgraduate education. Though public funding per unit of student load rose from the 1989–90 low, the 1996 Vanstone budget set in train a new series of spending cuts; and while outlays on fixed capital and equipment, and total student assistance payments, both increased significantly during the decade, government final consumption expenditure remained below the 1977–78 level.

Overall, between 1975–76 and 1997–98 real GDP increased by 101.5 per cent, and student load in higher education increased by 127.9 per cent, while publicly financed investment in higher education rose by 26.1 per cent in real terms. Public final consumption expenditure reached an historic low of \$5518 per student in 1997–98, only 47.2 per cent of the 1975–76 level. In 1997–98 total public investment was 0.89 per cent of GDP. In 1998–99 the ABS

Table 2 Government Outlays on Higher Education Per Unit of Student Load, Australia: 1975–76 to 1997–98

| Year    | Government outlays per unit of student load              |   |                                   |
|---------|--|---|-----------------------------------|
|         | Student load expenditure (average of two calendar years) | Final consumption expenditure (\$ 1989–90 prices) | Total outlays (\$ 1989–90 prices) |
| 1975–76 | 228950   | 11683   | 15307                             |
| 1980–81 | 251450   | 11449   | 13158                             |
| 1985–86 | 282359   | 10484   | 11871                             |
| 1990–91 | 399543   | 6554  | 9101                              |
| 1995–96 | 475032   | 5722  | 9123                              |
| 1997–98 | 521783   | 5518  | 8471                              |

Note: Total outlays includes student assistance (unlike Table 5).

Source: Revised and unpublished data from the ABS.

shifted the public finance collections to accruals accounting and series continuity was lost. Data from the ABS indicate that in 1998–99 there was a further decline of 2.3 per cent in total government funding of higher education (excluding personal benefits), and a 5.0 per cent drop in the level of government funding per unit of student load.

### 3. Department of Education, Training and Youth Affairs Data on Public and Private Investment since 1989

Changes in the incomes and expenditures of higher education institutions from 1989 can be tracked in the data collections of the Commonwealth Department of Education, Training and Youth Affairs (DETYA: these data exclude 'off-budget' items such as some revenues of university-controlled companies). The Dawkins reforms remade higher education as a competitive system of self-managing institutions with control over their own resources, while subject to accountability requirements and limits on numbers in relation to government-funded places. The underlying objectives of the shift to mixed funding were to provide fiscal relief for the government, and to strengthen economic relationships between universities

and industry so that higher education would contribute to national competitiveness. The first objective was successfully achieved. The HECS was introduced in 1989 at an average 20 per cent of course costs; later, in several stages, the level and rate of repayment were increased. The DETYA data also record a rapid increase in incomes from international student fees, vocational postgraduate fees, especially in Business Studies, and continuing education (Table 3). The number of international students grew from 21 112 in 1989 to 83 111 in 1999. The new autonomous institutions moved more quickly than expected, though from the policy viewpoint this autonomy and responsiveness had downsides that became apparent later.

By 1998, 33.2 per cent of all income received by higher education institutions was derived from the HECS plus university-determined fees and charges, compared to about 2 per cent derived from fees and charges in 1983. In 1998 income from international students constituted 8.3 per cent of all income, and more than one dollar in five in institutions with greatest exposure to the market. Whereas governments provided 90 per cent of funding in 1983 and 70.3 per cent in 1989, by 1998 the public share was down to 51.9 per cent (Table 4). Though most OECD countries saw increases in private

Table 3 Income of Higher Education Institutions by Source, Australia: 1989 to 1998  
(\$million 1989–90 prices)

| Year | Governments | HECS     | International student fees | Domestic student fees (award courses) | Other fees and charges <sup>a</sup> | Donations and endowments | University investments | Other   | Total    |
|------|-------------|----------|----------------------------|---------------------------------------|-------------------------------------|--------------------------|------------------------|---------|----------|
| 1989 | 3090.279    | 501.773  | 66.281                     | 7.110                                 | 185.513                             | 140.578                  | 231.115                | 174.103 | 4396.752 |
| 1990 | 3272.274    | 562.518  | 136.714                    | 11.962                                | 251.423                             | 110.260                  | 252.357                | 183.560 | 4781.068 |
| 1991 | 3509.671    | 613.520  | 207.671                    | 18.602                                | 289.723                             | 108.632                  | 226.309                | 275.186 | 5249.316 |
| 1992 | 3620.920    | 746.701  | 269.239                    | 26.027                                | 289.896                             | 102.001                  | 201.120                | 395.041 | 5650.946 |
| 1993 | 3646.860    | 786.950  | 317.217                    | 36.780                                | 350.548                             | 94.396                   | 206.223                | 607.260 | 6046.234 |
| 1994 | 3949.751    | 811.146  | 355.376                    | 50.671                                | 279.607                             | 60.508                   | 119.741                | 734.917 | 6361.718 |
| 1995 | 4008.887    | 819.669  | 400.938                    | 67.032                                | 332.033                             | 77.514                   | 277.185                | 864.285 | 6847.543 |
| 1996 | 4170.021    | 831.725  | 473.571                    | 80.186                                | 407.397                             | 75.120                   | 265.904                | 875.373 | 7179.297 |
| 1997 | 3972.290    | 1064.754 | 552.238                    | 99.865                                | 427.846                             | 90.256                   | 287.302                | 739.295 | 7233.846 |
| 1998 | 3834.152    | 1268.901 | 613.027                    | 141.784                               | 430.876                             | 100.180                  | 261.139                | 744.512 | 7394.571 |

Note: (a) This includes fees for non-award continuing education courses, and part of fee-for-service research and consulting income (the remainder of research and consulting activities is included under 'other').

Source: DETYA, Higher Education data collection.

Table 4 Income of Higher Education Institutions by Source, Australia: 1989, 1995, 1998  
(per cent)

| Year | Governments | HECS  | Fees and charges | Donations | Investments | Other | Total  |
|------|-------------|-------|------------------|-----------|-------------|-------|--------|
| 1989 | 70.29       | 11.41 | 5.89             | 3.20      | 5.26        | 3.96  | 100.00 |
| 1995 | 58.54       | 11.97 | 11.68            | 1.13      | 4.05        | 12.62 | 100.00 |
| 1998 | 51.85       | 17.16 | 16.03            | 1.35      | 3.53        | 10.07 | 100.00 |

Source: DETYA, Higher Education data collection.

funding during this period (Williams 1992), the Australian change was remarkable in its speed and universality.

In policy terms, Treasury was the chief winner. The main funding change was the transfer of part of the cost of investment in education from government to students, coupled with the lowering of fiscal expectations and raising of efficiency pressures within the universities. The creation of productive education-industry links was less successful. In 1998, of an estimated \$2.6 billion spent on research and development in higher education, only \$0.136 billion (5.2 per cent) was financed by business enterprises. The Cooperative Research Centre program, designed to facilitate university-industry collaboration, was mostly fruitful in research terms but was largely funded by government and universities. While Australia became the third largest global provider of international education, this did not in itself signify an expanded national capacity to do business in Asia, apart from education business. Given that in the 1990s universities proved highly responsive to market opportunities, explanations for their failure to secure a greater level of industry investment must lie partly on the industry side. At the same time, the erosion of university capacity and energies, brought about by the coupling of rapid entrepreneurial development to declining public investment per student, intensified cost pressures and a reduced capacity for basic research, probably impaired the attractiveness of universities as sites for industry investment.

#### 4. Funding after 1995

From 1996 the policies of the Howard Government concentrated and intensified certain

trends of the post-Dawkins period. Whereas the early 1990s saw an expansion of both public and private investment, in the context of a growing higher education system and institutions that had assumed both a wider range of functions and the task of reinvention (Marginson and Considine 2000); between 1995 and 1998 public investment fell sharply and there was a 5.6 per cent decline in total income per student, despite a major increase in private investment (Table 5). Corporate universities were required to again step-up their entrepreneurial activities, though now from a diminishing total resource base, strengthening the emphasis on short-term revenue-raising.

Between 1995 and 1998 total public funding fell by 4.4 per cent and public funding per unit of student load fell by 16.4 per cent (Tables 3 and 5). Revenue from the HECS rose by 54.8 per cent, and international student income by 52.9 per cent, and there was a 111.5 per cent growth in direct fee income from domestic students, including a small component of fee-paying undergraduates from 1998. The growth in HECS funding was largely cancelled out by the decline in government operating grants. Between 1995 and 1998, income from these two sources of core funding, taken together, rose by only 5.7 per cent in total terms and in terms of student load fell by 7.4 per cent, from \$10449 (1995) to \$9650 (1998).

Consequently domestic student load grew slowly, despite the 1996 policy decision, copied from the United Kingdom, to fund enrolments additional to planned load at the HECS rate. Meanwhile international student load jumped from 39367 (1995) to 68109 (1998), so that almost half of total growth in student load in universities was in international students (Table 6). The now autonomous

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**Table 5 Income of Higher Education Institutions Per Unit of Student Load, Compared to Student-Staff Ratio, Australia: 1989 to 1998**

| Year | Student load | Income per unit of student load, from:       |   |  | Student-staff ratio <sup>a</sup> |
|------|--------------|--|---|--|----------------------------------|
|      |              | Governments<br>(\$million<br>1989-90 prices) | Governments<br>plus HECS<br>(\$million<br>1989-90 prices) | All sources<br>(\$million<br>1989-90 prices) |                                  |
| 1989 | 354235       | 8724   | 10140   | 12412  | 12.81                            |
| 1990 | 376522       | 8691   | 10185   | 12698  | 12.81                            |
| 1991 | 422563       | 8306   | 9758  | 12423  | 13.49                            |
| 1992 | 433005       | 8362   | 10087   | 13034  | 14.69                            |
| 1993 | 441085       | 8268   | 10052   | 13708  | 14.50                            |
| 1994 | 444406       | 8888   | 10713   | 14315  | 14.53                            |
| 1995 | 462087       | 8676   | 10449   | 14819  | n.a.                             |
| 1996 | 487977       | 8548   | 10250   | 14712  | 15.31                            |
| 1997 | 514727       | 7717   | 9786  | 14054  | 16.75                            |
| 1998 | 528838       | 7250   | 9650  | 13983  | 17.38                            |

Note: (a) Units of student load per effective full-time teaching-related staff member (including casual staff).

n.a. means data are not available. Teaching-related staff includes teaching only and teaching/research staff; it excludes research-only staff.

Source: DETYA, Higher Education data collection.

**Table 6 Growth in Higher Education Student Load Compared to Growth in Income, International and Domestic Students, Australia: 1995 to 1998**

|  | 1995             | 1998             | Change between<br>1995 and 1998<br>(per cent) |
|--|------------------|------------------|---|
| Fee income from international students | \$400.9 million  | \$613.0 million  | +52.9   |
| International student load             | 39367            | 68109            | +73.0   |
| Income from governments and the HECS   | \$4828.6 million | \$5103.1 million | +5.7  |
| Domestic student load                  | 422720           | 460474           | +8.9  |

Note: Income data are in 1989-90 prices.

Source: DETYA, Higher Education data collection.

universities were following the logic of the policy-determined incentives that they faced: incentives with clear and predictable outcomes. Universities naturally gave priority to recruiting international students, where numbers were open-ended and each place was fully funded. In the case of domestic students planned load was funded on a declining basis and below full cost, while additional load was funded at marginal cost.

The same incentive framework also ensured that growth took place in courses where the ap-

parent private benefits were greatest and direct revenues were readily obtained; not necessarily in courses where investment created the maximum long-term national benefits and facilitated the global 'knowledge economy'. Public policy no longer intervened in the balance between disciplines, and universities were free to play with this balance as they saw fit. The losers were disciplines that did not create immediate vocational benefits; the winners were Business Studies and Computing. From a university manager's point of view, Business

courses were also relatively cheap to provide, requiring little technological input or research expertise, and could be taught by casual staff in temporary accommodation. Between 1995 and 1998, the number of Business graduates grew by 42.7 per cent while graduations in all other fields rose by 7.1 per cent, and only 3.7 per cent among domestic students (Table 7). International student load in coursework Masters programs increased from 4049 in 1995 to 14243 in 1998, by which time international students constituted 42.0 per cent of all student load at this level.

Often, postgraduate course content was similar to that of undergraduate programs. In this manner Australian university revenue was augmented by global credentialism: a growing number of East and South-East Asian families used English-language postgraduate degrees to facilitate entry into cross-national business circles. From the viewpoint of Australian public policy, it was a less than optimum form of internationalisation in education. For the most part, the public and private educational goods created in coursework international degrees were lost to Australia when students returned to their home countries. This contrasted with research degrees, where international students created knowledge feeding into the domestic

academic system and was often useful to local industry; and there were longer term spin-offs via skilled migration and collaboration in research. Yet between 1995 and 1998 international student load in research degrees rose only modestly, from 3665 to 4197. In 1998 research students constituted only 5.4 per cent of all international student load; while international students constituted 14.5 per cent of all research student load, significantly less than in pre-1989 Australia and in the contemporary United States and United Kingdom where international research students continued to sustain a strong presence.

### 5. Resources Underlying the Quality of Teaching and Research

The quality of teaching and research in higher education eludes a single comprehensive measure, but some of the conditions affecting quality can be tracked. Staffing indicators derived from the DETYA data indicate that in the 1990s there was potential for quality decline. In 1998 the overall ratio of effective full-time teaching staff, including casuals, to student load was 17.4, compared to 12.8 in 1989 (Table 5). The overall ratio increased at the beginning of the 1990s, stabilised, and then increased

Table 7 Growth in the Number of Graduates, Higher Education, Australia, International and Domestic Students: 1995 to 1998

|                                 | 1995   | 1998   | <i>Change in the number of graduates between 1995 and 1998</i> |         |
|---------------------------------|--------|--------|--|---------|
| International student graduates |        |        |  |         |
| Business Studies                | 6342   | 13497  | +7155  | +112.8% |
| All other disciplines           | 7580   | 11633  | +4053  | +53.5%  |
| Total                           | 13922  | 25130  | +11208   | +80.5%  |
| Domestic student graduates      |        |        |  |         |
| Business Studies                | 23622  | 29268  | +5646  | +23.9%  |
| All other disciplines           | 103449 | 107286 | +3837  | +3.7%   |
| Total                           | 127071 | 136554 | +9483  | +7.5%   |
| All graduates                   |        |        |  |         |
| Business Studies                | 29964  | 42765  | +12801   | +42.7%  |
| All other disciplines           | 111029 | 118919 | +7890  | +7.1%   |
| Total                           | 140993 | 161684 | +20691   | +14.7%  |

Source: DETYA, Higher Education data collection.

more sharply after 1995. Remarkably, student-staff ratios rose by almost as much in the boom areas of Business Studies and Computing, as in Education, the Arts, the Humanities and the Social Sciences. In addition, the proportion of teaching that was handled by casual staff increased throughout the 1990s, reaching almost one-fifth in 1998 (Table 8).<sup>2</sup>

This dramatic deterioration in student-staff ratios creates the apparent paradox which is set down in Table 5. Between 1989 and 1998, total funding per unit of student load increased by 12.7 per cent; and while government funding plus HECS per unit of student load fell, it was only by 4.8 per cent. Yet the academic staffing ratio deteriorated by 26.3 per cent. Why this divergence between the funding trend and the staffing trend?

The explanation that follows is more speculative than the rest of this article. During the 1990s the value of Australian academic salaries rose slightly in real terms. Further, the annual costs of an aging staff structure increased, *ceteris paribus*, due to promotion and incremental movement. Unlike the 1980s it was not possible to sustain student-staff ratios by running down the value of salaries. More fundamentally, universities spent a decreasing proportion of their total resources on teaching-related activities, due to the change in their character as institutions. The Dawkins reforms transformed the universities, from independent-minded branches of the public service, underpinned by long-term public investment and with objectives defined in terms of an 'arms-length' public policy, to 'Enterprise Universities' (Marginson and Considine 2000), whose ulti-

mate horizon was not teaching, research or national needs, but the institutional interests of the university as an end in itself. Not quite public corporations, they became public enterprises, driven increasingly by the need for short-term revenues. A growing part of university resources was devoted to the functions that sustained competitive advantage and augmented fee-based incomes: offshore operations, marketing, public relations, communications, asset management, alumni fund-raising and so on. One sign of the shift in priorities was that between 1989 and 1998 the proportion of total staffing that was employed in teaching-related positions fell from 41.0 to 37.7 per cent; while surveys of academic staff found an increasing proportion of the time of teaching-related staff was in fact devoted to administration and resource raising (for example, McInnis 2000).

Thus the picture created by the macro-trend in incomes is radically incomplete, failing to take into account the distribution of resources between different functions, and the change in the pattern of expenditures amid the incentive structure brought about by the Dawkins funding regime and reinforced by the Vanstone cuts. New private incomes failed to fully substitute for lost public incomes. Commercial revenues were largely absorbed in the costs of generating them, and in some universities fee-based courses were subsidised from government and HECS funding. In other cases market incomes were used to sustain the 'ongoing' academic infrastructure, reinforcing shifts from basic to commercialisable research, and from basic academic disciplines to market-segmented vocational applications.

Table 8 Staff in Higher Education, Australia: 1989 and 1996 to 1998

| Year | Student load | Effective full-time (EFT) staff |       | Proportion of EFT staff time that was casual |                  | Proportion of total EFT staff time (includes casual) employed in teaching-related positions (per cent) |
|------|--------------|---------------------------------|-------|--|------------------|--|
|      |              | Teaching-related                | Other | Teaching-related (per cent)                  | Other (per cent) |  |
| 1989 | 350137       | 27326                           | 39255 | n.a.   | n.a.             | 41.04  |
| 1996 | 514727       | 31877                           | 51221 | 17.49  | 9.41             | 38.36  |
| 1997 | 528838       | 30731                           | 50736 | 18.10  | 10.29            | 37.72  |
| 1998 | 544146       | 30424                           | 50315 | 19.35  | 10.49            | 37.68  |

Source: DETYA, Higher Education data collection.



## 6. Comparative International Funding

In Australia in 1998, 81.6 per cent of 15–19 year olds were enrolled in education, higher than the US rate of 74.2 per cent, though below most of Western Europe. Between 1990 and 1997 the rate of Australian tertiary enrolment increased by 31 per cent, compared to 8 per cent in the United States and an average 49 per cent in OECD countries. Australia had a relatively high proportion of students studying part-time,<sup>3</sup> and the data should be discounted for international students: this weakens the comparative performance.<sup>4</sup> In terms of funding, in 1997 Australia invested 5.6 per cent of GDP from all sources on education and training, down from 6.0 per cent in 1993 and well below the 1997 OECD mean of 6.1 per cent.<sup>5</sup> In tertiary education, the comparison is less

disadvantageous to Australia, but the trend is similar. Table 9 shows that Australian public investment fell from just above the OECD mean in 1993 to the OECD mean of 1.0 per cent of GDP in 1997, and was still falling (Table 1). Private investment was higher than in most countries but the same as the OECD mean (0.7 per cent of GDP) because of the weight of the United States. Both US public investment (1.4 per cent) and private investment (1.2 per cent) are well above Australian levels (OECD 2000).

Thus in comparative international terms, the Australian investment in education is no longer superior, and is deteriorating relative to the OECD region. Australia combines relatively high rates of participation with weakening public investment and the growing production of private goods relative to public goods. After a

**Table 9 National Investment in Tertiary Education as a Proportion of GDP, Public and Private Sources, Australia and Selected OECD and Other Countries: 1993 and 1997**  
(per cent)

| Country        | 1993           | 1997           | 1997            | 1997        |
|----------------|----------------|----------------|-----------------|-------------|
|                | Public sources | Public sources | Private sources | All sources |
| Finland        | 1.8            | 1.7            | 0.1             | 1.7         |
| Canada         | 1.7            | 1.2            | 0.8             | 2.0         |
| Norway         | 1.5            | 1.3            | 0.1             | 1.4         |
| Sweden         | 1.5            | 1.6            | 0.1             | 1.7         |
| Denmark        | 1.3            | 1.1            | 0.1             | 1.2         |
| Netherlands    | 1.3            | 1.1            | 0.1             | 1.2         |
| New Zealand    | 1.2            | 1.0            | n.a.            | n.a.        |
| United States  | 1.2            | 1.4            | 1.2             | 2.6         |
| Austria        | 1.1            | 1.3            | 0.2             | 1.5         |
| Australia      | 1.1            | 1.0            | 0.7             | 1.7         |
| Ireland        | 1.0            | 1.0            | 0.4             | 1.4         |
| France         | 0.9            | 1.0            | 0.2             | 1.2         |
| Germany        | 0.9            | 1.0            | 0.1             | 1.1         |
| Italy          | 0.8            | 0.6            | 0.2             | 0.8         |
| Spain          | 0.8            | 0.9            | 0.3             | 1.2         |
| United Kingdom | 0.7            | 0.7            | 0.3             | 1.0         |
| Japan          | 0.4            | 0.5            | 0.6             | 1.1         |
| Korea          | 0.3            | 0.5            | 2.0             | 2.5         |
| OECD total     | 1.0            | 1.0            | 0.7             | 1.7         |
| Malaysia       | n.a.           | 1.1            | 0.3             | 1.4         |
| Thailand       | n.a.           | 1.0            | n.a.            | n.a.        |

Source: OECD (2000).

general reduction in the GDP share devoted to education in the 1980s and early 1990s, half the OECD countries are now increasing the proportion of GDP devoted to higher education, mostly via public investment. National success stories such as Finland are partly grounded in education, research and software development. The United States sustains a strong policy focus on research and development, and Canada has undertaken a major new investment in research (Batterham 2000).

## 7. Concluding Comments

The logic of 1990s policy was that of the invisible hand: universities driven by self-interest would together constitute the optimum national interest in higher education. At the same time the 'national interest' was redefined, to give priority to fiscal relief over the long-term benefits derived from investment in economic and social infrastructure, so that the aggregate outcome was not to augment productive capacity but to reduce costs.

As a result, the Commonwealth secured fiscal relief, and export revenues, while the growth of commercial incomes ensured that the total income of universities was more than sustained, at least until 1996. Continued but slowing enrolment growth was secured by thinning out the core resource base of the sector. The price was a deteriorating teaching and research infrastructure, coupled with the forced focus of much of university development around a narrow band of activities, especially fee-based coursework in Business for international students. In formal terms, policy was now indifferent to these trends. The maintenance of quality and the balance between fields of study were matters for universities themselves to determine. Although institutions remained heavily dependent on government funding, they were unable to draw attention to their resource problems without jeopardising their market position. Quality assurance systems, implemented at government behest, failed to identify trends in the resource conditions underlying quality, but helped to cover up the effects. It was clever politics. In terms of long-term economic outcomes it was less attractive,

a flawed basis for entering the global knowledge economy (OECD 1999).

If national investment in higher education returned to the GDP share of the 1975–76 level in Australia—still well short of the US level of investment today—another \$4 billion would be sunk into education and research. In this context the 29 January Commonwealth statement on innovation (Howard 2001) was a modest step, providing for an additional \$159.4 million in the first year and \$946.6 million per annum after five years. The package offered a significant increase in funding for scientific research, little for industry research and development, and left public operating grants to universities unchanged. The Government also announced that it would subsidise domestic postgraduate fees via the HECS mechanism, with fees determined by the universities. The most likely outcomes were that universities would shift more of their scarce resources into a narrow range of marketable courses; and the strong 'sandstone' universities would charge high prices, reaping the benefits of their 'positional' status without necessary improvement in efficiency, course quality or responsiveness to 'customers' (Marginson 1997b). Thus the public would underwrite the production of private goods for individuals and universities. Arguably, public investment in higher education would be more efficiently devoted to the creation of public goods. The same subsidy would generate a better outcome if applied to operating grants, directly addressing the problems of quality and capacity.

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## Endnotes

1. Student load is a measure of effective full-time student units.
2. There is some evidence that the quality of the learning experience deteriorated in other ways. Between 1987 and 1999 the proportion of full-time students in higher education who were working part-time expanded significantly. Among 18 year olds, labour force participation rose from 44.7 to 65.2 per cent, and

the proportion in work rose from 34.9 to 55.2 per cent (ABS 2000b). Some combinations of work and study are educationally desirable, but most of such jobs simply cut into the time available for study.

3. In 1998 the average 17 year old in Australia could expect 1.7 years of full-time education and 1.4 years of part-time education, compared to 2.0 years full-time and 0.3 years part-time in the OECD as a whole (OECD 2000).

4. OECD data show that in 1998 Australia had the second highest rate of enrolment of international students in higher education (12.6 per cent), behind only Switzerland (15.9 per cent).

5. The 1997 level in the United States was 6.9 per cent and in Canada it was 6.5 per cent.

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**Policy Forum: Higher Education Funding****Australian Higher Education: Budgetary and Political Realities**

Andrew Norton\*

The Centre for Independent Studies

**1. Introduction**

Australia's universities and their lobby groups stand by their long-held view that more public funding will solve their financial problems. The Australian Vice-Chancellors' Committee, representing all but one of Australia's Vice-Chancellors, calls for an 'ongoing additional \$1 billion' (AVCC 2000c, p. 3). The National Tertiary Education Union, representing staff, suggests spending increases totalling around \$2.5 billion (NTEU 2001, pp. ii-iii). The National Union of Students is less specific, but wants 'free' education which would cost others about \$1.7 billion a year and the reversal of funding cuts that they (erroneously) put at \$1 billion (NUS 2001).

These demands, though, represent the triumph of hope over experience. Since the Hawke Government came to power in 1983 per student annual Commonwealth expenditure on higher education has declined almost every year. According to the AVCC's statistics, by 1999 the average annual payment was down 19.7 per cent since 1983. This trend has been bipartisan, with 15.1 per cent lost by the time the Coalition returned to power in 1996 (AVCC 2000a, Table A.2).<sup>1</sup> Even the Commonwealth Government's much-publicised January 2001 'innovation action plan for the

future', *Backing Australia's Ability*, offered no increase in general per student funding.

The universities have, so far, coped. Per student costs were curtailed with higher student:staff ratios, and many more fee-paying students, especially from overseas, were enrolled. There are signs, though, that this coping cannot continue. The accounting firm Deloitte Touche Tohmatsu has analysed universities' accounts over a number of years to determine their 'safety margin', the percentage by which revenue exceeds expenditure. Between 1996 and 1999 the sector's safety margin declined from 6.0 per cent to 3.3 per cent, with five universities recording negative safety margins in 1999 (Kemp 2001, p. 59). This situation can only get worse under current policies. The latest round of enterprise agreements will see pay rises of between 12.6 per cent and 14.7 per cent over the next few years (NTEU 2000). As salaries make up 60 per cent of university expenditure this is a very substantial increase in costs. As year by year the increments add up, more universities will slip into deficit.

**2. Government Incentives**

Of course the AVCC, the NTEU and the NUS believe this slide toward insolvency can and will be reversed through infusions of public money. As no government wants an embarrassing university bankruptcy, they are probably right that public money will keep universities afloat. Where they are wrong, I think, is in believing that governments will provide adequate, long-term funding for Australia's

\* The author was formerly Higher Education Adviser to Dr David Kemp. He is currently writing a Centre for Independent Studies monograph on higher education reform.

universities. We can see why they are wrong by looking at the pressures and incentives facing the Commonwealth Government.

Both major political parties are committed to fiscal responsibility in the interests of long-term economic prosperity. The Coalition has run Budget surpluses since 1997–98 and plans to continue them through the forward estimates period to 2003–04 (Department of Finance and Administration 2000). Opposition leader Kim Beazley says that for 'Labor, fiscal responsibility means that governments do not borrow to finance current spending. It means that they save in the good times so that over the cycle the budget balances' (Beazley 1999). If current growth forecasts are correct, this commitment would see Labor maintain surpluses if returned to power in 2001.

Fiscal responsibility has been difficult to achieve because real health, education and welfare expenditure has grown faster than either GDP or taxes for most of the time since the Whitlam Government (Warby and Nahan 1998, p. 4). Despite all the complaints about Howard Government 'cuts', it has in real terms increased overall expenditure per head by 3 per cent over the Keating Government, and spends 70 per cent more per head than the Whitlam Government (Warby 2000, p. 378). An ageing population creates significant long-term upward pressure on health and social security costs (Guest and McDonald 2000). Fiscal responsibility will continue to require strong Budget discipline.

### 2.1 Unpopularity of Tax

Of course fiscal responsibility allows for increases in expenditure provided it is financed from taxation or reallocating expenditure from other areas. Mark Latham is a rare individual who nominates cuts, to industry assistance and 'passive welfare' social security (Latham 2001, p. 27). For others, increased taxation is at least the implicit suggestion. That taxes and spending have not risen enough is attributed to ideology. Advocates of higher public funding such as Simon Marginson, for example, argue that 'despite the neo-liberal consensus in government the public funding of universities con-

tinues to enjoy popular support. The evidence of opinion polls and other surveys suggests a strong and consistent rejection of higher fees and reductions in government funding' (Marginson 1998, p. 4).

If people are just asked about fee levels, in isolation from issues of tax, Marginson is correct. For example, a 1997 Morgan poll asked voters whether they were satisfied with the government's increase in HECS charges. Sixty-eight per cent said they were dissatisfied, and only 22 per cent said they were satisfied (Morgan Poll 1997). If, however, voters are asked to choose between government spending more on social services or reducing tax they consistently choose lower tax. This choice has been put to voters over time by the Australian Election Survey. In 1993, 56 per cent favoured less tax and 17.3 per cent preferred more services. In 1996, 57.1 per cent favoured less tax, and 16.8 per cent preferred more social services. In 1998, perhaps reflecting changed sentiment after the 1996 Budget, 46.9 per cent favoured less tax, and 25.6 per cent favoured more services. Even with this reversal of the trend, there were still many more people in favour of reducing tax than there were in favour of spending more on social services (Social Science Data Archive 2000). Spending on universities may be less popular than spending on other social services. A 1994 survey on public expenditure asked its respondents to prioritise the areas on which they wanted extra spending. Spending on primary and secondary schooling was a much greater priority than spending on universities (Withers, Throsby and Johnston 1994, p. 36). These surveys are more realistic than those cited by people supporting increased public higher education spending. They recognise that a dollar spent on universities is a dollar that cannot be spent on something else, and encourage survey respondents to make choices rather than wish lists.

The surveys also accord with the political experience that raising taxes is not the way to find favour with voters. A Morgan poll in October 1998 found that more than half the voters surveyed were concerned the GST would cause their family to pay more tax (Morgan Poll 1998). In mid-June 2000, just prior to the

introduction of the GST, the Morgan poll found that primary vote support for the Coalition had fallen to its then lowest point since the Liberal Party was founded, 33.5 per cent, with 40 per cent two-party preferred (Morgan Poll 2000). While obviously voter concerns extended beyond GST costs, these are hardly comforting figures for politicians contemplating a heavier tax burden.

## 2.2 Electoral Irrelevance

Politicians' reluctance to spend big on higher education also reflects the realities of how many people are directly affected by universities compared to how many are directly concerned with competing spending priorities. Just within the education area, students and staff in primary and secondary schools outnumber students and staff in universities by about five to one (Australian Bureau of Statistics 2000, pp. 266, 270–1). Recipients of social security outnumber university students and staff by more than seven to one (Australian Bureau of Statistics 2000, p. 186). Medicare processes about ten items per year per person (Australian Institute of Health and Welfare 2000, p. 300). Even larger numbers would think they might need health and welfare services, whereas many people never go to university, and most of those who do are there for four years or less, covering only one or two elections.

Attempts by the higher education lobbies to make themselves electorally important have not met with much success. A poll done before the 1996 election found that even among 18–24 year olds only 28 per cent nominated 'Education/schools' in their top three issues, and only 6 per cent nominated HECS/Austudy (Morgan Poll 1996). The 1998 election was won by the Coalition despite continual criticism from higher education lobbies. In October 1999, with virulent denunciation of Dr Kemp's leaked plans to reform higher education, Coalition support actually went up by 0.5 per cent (Morgan Poll 1999).

Commentators like Simon Marginson, cited above, see neo-liberal ideological explanations for higher education funding shortfalls. I think the better explanation comes from the mundane

realities of government expenditure rising faster than revenue, and democratic governments delivering the services needed by the largest number of people. No matter how many critiques of 'neo-liberalism' are written, these budgetary and electoral realities will remain. Universities will always be less important than schools, social security and health.

## 3. Student Incentives

By contrast, students have incentives to finance higher education properly, wanting both the intellectual development it can offer and the higher earnings it can bring. American research indicates that spending more on higher education pays off in higher lifetime earnings (Borland et al. 2000, p. 22). It is reasonable to presume that the highest returns go to the most intellectually able, a presumption confirmed by the fact that high grades at university are linked to subsequent high earnings (Bowen and Bok 1998, p. 141).

While the development of intellectual ability is complex, a major survey of the literature found that 'substantial evidence exists to suggest that interactions with major socialising agents (faculty and peers) are, in fact, significantly linked to development of general cognitive skills during college' (Pascarella and Terenzini 1991, p. 149). Even leaving aside the matter of whether universities are able to offer salaries attractive to high quality staff, it is clear from steadily increasing student:staff ratios, escalating from an average of around 13 to 1 in 1990 to about 19 to 1 in 1999 (AVCC 2000a), that in Australia opportunity for interaction between students and staff must be declining, and with it the chance of students developing their intellectual abilities.

Australian survey evidence confirms that students perceive staff contact and input as a problem. The Course Experience Questionnaire (CEQ), sent to all completing students, asks whether they agree that staff put a lot of time into commenting on their work. Only 9 per cent strongly agree, and a further 25 per cent agree, though less strongly. The rest ranged from a neutral response to strongly disagreeing (Graduate Careers Council of Australia 2001,

p. 9). The problems show up even more clearly in a 1999 survey of first year students. While they think the academic staff are approachable (62 per cent agreeing), this seems to be only in the unlikely event that they can find them to approach, with 38 per cent saying that academic staff were usually available to discuss their work, a decline from 45 per cent in 1994. The response is poorer still on whether they get helpful feedback on their work (25 per cent) and whether most academic staff take an interest in their progress (21 per cent) (McInnis, James and Hartley 2000, p. 48).

It is in the interests of students to get student:staff ratios down. A practical way for students to invest more is through top-up fees, now supported by the Group of Eight, a lobby group consisting of the eight research-intensive universities (Group of Eight 2000, p. 19).<sup>2</sup> The Group of Eight's proposal has little detail, but the general idea is that instead of all the HECS charges going to the government, as is the case now, universities could levy additional charges payable to themselves. The top-up fees could still be deferred and repaid with an income-contingent loan. As about three-quarters of students are HECS-liable undergraduates, top-up fees would create a real link between costs and revenues, remedying a serious structural flaw in the current system.

To achieve maximum positive effect, top-up fees should be linked to deregulating the entire system, with enrolment patterns set by student demand, including letting in new competitors that meet quality assurance standards. This would reduce the opportunities for profiteering that exist in a quota-driven system, and more importantly allow greater diversity, including teaching-focused colleges. American research shatters the notion that there is a systematic positive link between research and teaching, whatever occasional benefits may be had. In a survey of 212 American higher education institutions, among those rated in the top 10 per cent for research not one is even average in its 'student orientation', defined in terms that include academics' interest in students' academic and personal problems and opportunities for student-faculty interaction. Even relaxing 'strong' to being in the top 35 per cent for stu-

dent orientation and research, only eight of the 212 made it (Astin 1999, p. 90). The situation is similar in Australia. The authors of *The Age Good Universities Guide* rank universities using data from the CEQ. Among the Group of Eight, none gets into the top 40 per cent (Ashenden and Milligan 2000).

#### 4. Objections to Fees

The traditional objection to fees is that they deter prospective students, especially from low-income groups, leaving us with the 'dumb rich'. If fees were up-front, this would be a possibility. Fees, however, would not be up-front in the Group of Eight's proposal. The argument against fees has to default to the claim that low-income students are debt-averse. There is little empirical evidence to support this view. The only serious study of debt aversion found that 'the SES background of groups had no strong or consistent effect on the level of debt aversion as measured by their willingness to apply for new mortgages or personal loans and the amounts involved' (Andrews 1999, p. 17).

The existing HECS system provides evidence that Andrews' assessment is right. The proportion of young people of low socioeconomic status attending university increased nearly 70 per cent over the period in which it went from being free to having HECS charges attached (Norton 2000, p. 5). Overall demand did drop slightly after a substantial increase in HECS charges starting in 1997 (Kemp 2000, p. 43). It is unclear, though, that this was directly related to price increases. A simultaneous reduction in the income level at which HECS debt must be repaid, effectively requiring most students with full-time jobs to begin repaying immediately, is the more likely cause, especially as reduced demand was concentrated in the mature age group. Whatever the cause, applications resumed growth in 1999 and 2000 (AVCC 2000b, Table C.3), suggesting that students are willing to pay higher prices, even when, as with the HECS increase, prices were rising without any compensating increase in service levels.

All this suggests low-income groups are not as economically irrational as some presume. Increasing numbers correctly saw that higher

education offered better paid, more interesting and less vulnerable jobs, and sensibly took on debt that was a small portion of their increased lifetime earnings (Borland et al. 2000).

## 5. Conclusion

Whatever the philosophical arguments for more public spending, the more pressing need is to put in place policies that will reliably deliver enough money to run a quality higher education system. Given the incentive structures discussed in this article, allowing universities to charge top-up fees is a necessary prudential part of such a change. This does not preclude universities from arguing for higher subsidies. What it does preclude is calls for more public spending being the higher education sector's major political strategy. It is just too risky. In fact it is worse than risky. It is a gamble they have already lost almost every year since before some of 2001's first year students were born.

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## Endnotes

1. This situation, it should be said, is partly due to the effects of the quota system. Each university receives from the Commonwealth Government a set number of so-called fully funded places. For these places the subsidy is down only 8.2 per cent since 1983, and has actually gone up slightly under the Coalition (AVCC 2000c, Table A.2). The larger drop is due to so-called over-enrolments, students taken above quota, for which the universities receive about \$2600 each. These students push down the average subsidy.

2. The Group of Eight still supports more public funding, especially for research, but has made a break with the old-style lobby groups on the issue of undergraduate funding.

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